

**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas**  
Independent Auditor's Report and Financial Statements  
December 31, 2015 and 2014



**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas  
December 31, 2015 and 2014**

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## Independent Auditor's Report

Board of Trustees  
South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
Arkansas City, Kansas

We have audited the accompanying balance sheets of South Central Kansas Regional Medical Center d/b/a South Central Kansas Medical Center, a component unit of the City of Arkansas City, Kansas, as of December 31, 2015 and 2014, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise South Central Kansas Regional Medical Center d/b/a South Central Kansas Medical Center's basic financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the provisions of the Kansas Municipal Audit and Accounting Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Central Kansas Regional Medical Center d/b/a South Central Kansas Medical Center as of December 31, 2015 and 2014, and changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As discussed in Note 1 to the financial statements, in 2015 the Hospital adopted Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*. Our opinion is not modified with respect to this matter.

### ***Other Matters***

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and pension information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Supplementary Information*

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*BKD, LLP*

Wichita, Kansas  
July 7, 2016

**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas  
Management's Discussion and Analysis  
Years Ended December 31, 2015 and 2014**

***Introduction***

This management discussion and analysis of the financial performance of South Central Kansas Regional Medical Center d/b/a South Central Kansas Medical Center (Hospital) provides an overview of the Hospital's financial activities for the years ended December 31, 2015 and 2014. It should be read in conjunction with the accompanying financial statements of the Hospital. The amounts reported in the management discussion and analysis for 2013 have not been restated for GASB 68 and 71.

***Financial Highlights***

- Cash decreased by \$53,963 or (7)% from \$746,413, the balance at the end of 2014, to \$692,450 on December 31, 2015. The previous year showed a decrease in cash of \$1,394,684 or (65)%.
- The Hospital's net position decreased \$1,840,931 in 2015. In 2014, net position decreased \$7,350,057, \$6,276,139 was due to implementation of GASB 68 and 71 and the reporting of the Hospital's portion of the net pension liability in the KPERS plan.
- The Hospital reported an operating loss of \$768,385 in 2015. In 2014, the Hospital reported an operating loss of \$366,447.
- Medicaid Disproportionate Share (DSH) payments of approximately \$699,000 were received in 2015, \$292,000 in 2014 and approximately \$65,000 in 2013.

***Using This Annual Report***

The Hospital's financial statements consist of three statements – a balance sheet; a statement of revenues, expenses and changes in net position; and a statement of cash flows. These statements provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The Hospital is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

***The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Position***

One of the most important questions asked about any Hospital's finances is "Is the Hospital as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses and changes in net position report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets, deferred outflows of resources, all liabilities and deferred inflows of resources using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The Hospital's total net position – the difference between assets, deferred outflows of resources, liabilities and deferred inflows of resources – is one measure of the Hospital's financial health or financial position. Over time, increases or decreases in the Hospital's net position are an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Hospital's patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors should also be considered to assess the overall financial health of the Hospital.

### ***The Statement of Cash Flows***

The statement of cash flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

### ***The Hospital's Net Position***

The Hospital's net position is the difference between its assets, deferred outflows of resources, liabilities and deferred inflows of resources reported in the balance sheet. The Hospital's net position decreased by \$1,840,931 in 2015 and decreased \$7,350,057 in 2014, as shown in Table 1.

***Table 1: Assets, Deferred Outflows of Resources, Liabilities, Deferred Inflows of Resources and Net Position***

	<b>2015</b>	<b>2014</b>	<b>2013</b>
	<i>(as restated)</i>		
<b>Assets</b>			
Cash	\$ 692,450	\$ 746,413	\$ 2,141,097
Sales tax funds - held by City	359,299	448,588	412,096
Patient accounts receivable, net	2,901,751	2,371,760	1,781,111
Other current assets	1,293,684	1,067,814	1,010,213
Restricted noncurrent cash and other assets held by City	2,000,119	2,442,520	2,436,659
Capital assets, net	24,675,467	26,026,023	27,501,061
Total assets	31,922,770	33,103,118	35,282,237
<b>Deferred Outflows of Resources - Pension</b>	252,600	276,174	-
Total assets and deferred outflows of resources	<u>\$ 32,175,370</u>	<u>\$ 33,379,292</u>	<u>\$ 35,282,237</u>
<b>Liabilities</b>			
Long-term debt	\$ 24,472,000	\$ 25,135,664	\$ 26,247,822
Other current and noncurrent liabilities	8,529,129	6,850,103	1,655,633
Total liabilities	33,001,129	31,985,767	27,903,455
<b>Deferred Inflows of Resources - Pension</b>	986,447	1,364,800	-
<b>Net Position (Deficit)</b>			
Net investment in capital assets	4,994,575	5,492,994	5,855,874
Restricted - expendable for			
Debt service	628,978	629,394	629,140
Capital acquisitions	100,000	100,000	100,000
Unrestricted (deficit)	(7,535,759)	(6,193,663)	793,768
Total net position (deficit)	<u>(1,812,206)</u>	<u>28,725</u>	<u>7,378,782</u>
Total liabilities, deferred inflows of resources and net position (deficit)	<u>\$ 32,175,370</u>	<u>\$ 33,379,292</u>	<u>\$ 35,282,237</u>

## ***Restricted Cash and Noncurrent Assets***

Under an agreement between the Hospital and the City of Arkansas City (City) related to the 2009 Hospital Revenue Bond issue (Capital Lease Obligation), the City's Public Building Commission (PBC) is acting as the trustee of the bond proceeds and paid contractor invoices as submitted. Funds held by the PBC as of December 31, 2015 and 2014, are primarily related to the bond reserve and unspent construction funds.

## ***Capital Assets***

In 2015, the Hospital invested over \$298,000 in equipment and upgrades. The major purchase in 2015 was for software upgrades to the Emergency Department system at \$168,700. Other software upgrades included the GE Centricity OB system at \$25,000. The Hospital also purchased a robot for the telehospitalist program at \$6,300, as well as new anesthesia pumps at a cost of \$10,000.

In 2014, the Hospital invested over \$286,000 in equipment and upgrades. The majority of the funds, \$149,000, were used to implement further technology for Meaningful Use Stage 2. Other purchased items included equipment for monitoring patients in ICU, new surgical procedure items and an upgrade to the drug dispensing machines in patient care areas.

In 2013, the Hospital purchased \$171,000 in equipment. Items included scopes for surgery, an anesthesia monitor and upgrades to computers, mammography and the nurse call system. The Hospital spent an additional \$23,000 in technology to implement the next phase of Meaningful Use. During 2013, the Hospital also assumed the costs related to utility improvements for the new hospital site and added \$2,833,501 related to land improvements as part of the capital lease with the City.

## ***Debt***

The Hospital, in conjunction with the City Manager of Arkansas City and Arkansas City Commission, obtained \$23,205,000 in revenue bonds. The debt is recorded as a capital lease obligation on the Hospital's books.

The Hospital's new 37-bed facility was envisioned to reflect the community's current and future medical needs. The facility allows for maximum flexibility for increasing outpatient services while providing for reduced acute care populations.

As a part of the development of the 168-acre Patterson Park subdivision where the Hospital is located, the City of Arkansas City established the infrastructure of streets, water mains and sewers. The City of Arkansas City has funded these with warrants and in 2013 issued General Obligation bonds for their financing. Consistent with the bond documents of the Arkansas City Public Building Commission, the Hospital agreed to pay special assessments related to extension of city utilities in the subdivision. As other property in the subdivision is sold or leased and developed, those parties will assume responsibility for the prorata share of special assessments and further, reimburse for the value of special assessments paid by the Hospital prior to the acquisition by the parties. Special assessments related to extension of city utilities for use by the Hospital totaled \$2,833,501. Payments are due monthly to the City and vary in amount based upon agreed payment schedule, see *Note 6* to the financial statements for specifics.

As of December 31, 2015 and 2014, the Hospital had \$24,272,000 and \$25,135,664, respectively, of capital lease obligations outstanding.



## ***Operating Results and Changes in the Hospital's Net Position***

The first component of the overall change in the Hospital's net position is its operating income or loss, generally, the difference between net patient service and other operating revenues and the expenses incurred to perform those services.

### ***Operating Margins***

The following are the major components of those changes.

- Total operating revenues increased \$331,768 over 2014, which is a 2% increase. Revenues increased \$895,644 from 2013 to 2014 or 6%. Total operating loss increased in 2015 by \$401,938, largely due to decreased electronic health records incentive revenue and increased expenses related to the addition of the downtown clinic. Operating loss decreased in 2014 and increased in 2013 by \$259,661 and \$886,792, respectively, largely due to the incentives from the Medicare and Medicaid programs for the adoption of Electronic Health Records.
- In 2015, the Hospital received approximately \$699,000 in DSH payments. This is an increase of 139% from 2014 with DSH payments at approximately \$292,000. DSH payments were \$65,000 in 2013. These payments are based on financial and statistical criteria and are related to costs incurred providing obstetrics and other services to low-income patients.
- Salaries and benefits increased approximately \$321,010 or 4% in 2015 due to bringing on the employees of the downtown clinic. The Hospital continues to pay for 50% of employee premiums for health insurance as well as a portion of dental premiums for a total cost of \$444,390. Also included in benefits is workers' compensation and state unemployment for a total of \$151,471. Salaries and benefits decreased approximately \$484,446 or 5% from 2013 to 2014 due to a decrease in patient volumes and outsourcing of dietary, housekeeping and laundry.
- In 2015, purchased services and professional fees increased 17% or \$508,068 due to outsourcing of previously employed positions. In 2014, these services increased 46% or \$944,384 as compared to 2013, due to outsourcing of previously employed positions.
- Other expenses include supplies, utilities, rentals and repairs and maintenance. In 2015, these amounts increased \$1,869. In 2014, these expenses increased 2% or \$81,931.
- The Hospital receives no ad valorem taxes through intergovernmental transfers from the City of Arkansas City.

**Table 2: Operating Results and Changes in Net Position**

	2015	2014	2013
	<i>(as restated)</i>		
<b>Operating Revenues</b>			
Net patient service revenue	\$ 16,660,152	\$ 15,845,931	\$ 14,499,906
Electronic Health Records Incentive revenue	297,142	790,854	1,139,442
Other operating revenues	85,937	74,678	176,471
Total operating revenues	17,043,231	16,711,463	15,815,819
<b>Operating Expenses</b>			
Salaries and wages and employee benefits	8,848,852	8,527,842	9,012,308
Purchased services and professional fees	3,524,218	3,016,150	2,071,766
Other operating expenses	3,789,431	3,787,562	3,705,631
Depreciation and amortization	1,649,115	1,746,356	1,652,222
Total operating expenses	17,811,616	17,077,910	16,441,927
<b>Operating Loss</b>	(768,385)	(366,447)	(626,108)
<b>Nonoperating Revenues (Expenses)</b>			
Interest income	42,317	53,247	44,697
Interest expense	(1,566,762)	(1,650,676)	(1,591,954)
Noncapital appropriations - City of Arkansas City - sales taxes	875,127	870,684	799,700
Noncapital grants and gifts	25,710	19,274	17,526
Transfer to City of Arkansas City	(448,938)	-	-
Total nonoperating revenues (expenses)	(1,072,546)	(707,471)	(730,031)
<b>Change in Accounting Principle - GASB No. 68</b>	-	(6,276,139)	-
<b>Decrease in Net Position</b>	\$ (1,840,931)	\$ (7,350,057)	\$ (1,356,139)

**Nonoperating Revenues and Expenses**

Nonoperating revenues and expenses has consisted primarily of interest income, interest expense and sales taxes. Interest income decreased \$10,930 from 2014 to 2015 and increased \$8,550 from 2013 to 2014. A half-cent sales tax supports the Hospital's operations and are being collected and maintained by the City until a transfer to the Hospital is needed.

In 2015, funds being reserved for the demolition of the old hospital building were transferred to the City. The Hospital transferred control of the building to the City in 2011. In 2015 the City paid to have the old hospital building demolished and removed.

**Capital Grants and Gifts**

The Hospital regularly receives gifts from the Hospital Auxiliary for capital purchases. Memorial funds and gifts through the "Building A Future of Excellence Campaign" have also been designated for the Hospital's use. The Hospital receives a bioterrorism grant to purchase items necessary for a disaster in the area from the Kansas Hospital Education and Research Foundation which is renewed annually.

In 2015, the Hospital was also awarded a grant under The Small Hospital Improvement Program (SHIP). This grant awarded funds to purchase education, training and software to help rural communities support a sustainable health care delivery system. This grant is offered by the Kansas Department of Health and Environment and can be renewed annually. The Hospital was awarded this grant in 2014 and 2013 as well.

### ***The Hospital's Cash Flows***

Changes in the Hospital's cash flows are consistent with changes in operating income and nonoperating revenues and expenses for 2015, 2014 and 2013, as discussed earlier. Net cash provided by the operating and noncapital financing activities of the Hospital were used to purchase capital equipment and pay debt service.

### ***Community Benefit***

It is commonly believed that a health care provider benefits the community which they serve. However, the definition of that benefit can vary greatly from one facility to the next. The Hospital bases the value of community benefit by measuring a variety of factors.

- **Facility Reinvestment** – Health care facilities must continually make investments in equipment to stay on top of the current and emerging health care needs of their communities. In 2015, 2014 and 2013, the Hospital invested nearly \$299,000, \$286,000 and \$171,000, respectively, in new equipment. In addition to the new equipment, the Hospital has constructed a new facility that will better serve the residents of the community as described in the debt section above. In addition to the equipment purchased in 2013, the Hospital assumed the cost of the utility improvements related to the new Hospital site of approximately \$2,300,000. This is being paid through a capital lease with the City and the Hospital's liability will be reduced by future developments at the Patterson Parkway site.
- **Percentage of Medicaid Patients Served** – In 2015, we attributed 17% of our inpatients as Medicaid recipients and 17% and 8% in 2014 and 2013, respectively. This is in contrast to the national average of 2%.
- **Charity Care** – \$379,815, \$298,953 and \$288,434 was written off in 2015, 2014 and 2013, respectively, for patients qualifying for approval through committee review. In general, our policy does not allow a charity care recipient to have an annual income of greater than two times the federal poverty guidelines. Our goal is to identify patients each year who qualify for charity care so those services can be properly classified as charity care and not reflected in our bad debt that was approximately \$1,300,000 in 2015.
- **Community Event Participation** – The Hospital participates in multiple events throughout the year, providing health information and free medical services such as mammograms, blood pressure checks and other free screenings for infants. The Hospital is also involved in employer health fairs, community health and safety fairs, and more specialized fairs such as the local birthing fair. The Hospital also sponsors the 2K run at the annual fall festival and various recreation league activities in the local community. Blood drives are also hosted five times a year at the Hospital and open to the community. In addition, the Hospital held its first 5K obstacle race in 2015. The race takes place on the land surrounding the Hospital and had 135 participants for the inaugural run.
- **Educational Opportunities** – The Hospital is a training site for multiple college nursing programs as well as physician assistant training. The Hospital is also a partner with the local college volunteer program. Also, as a partner in the county's health careers program, the Hospital provides hands-on experience for high school students interested in pursuing health care careers.

- **Health Information** – Multiple seminars, classes and health announcements are provided every year by the Hospital. Seminars continue to be given by the Hospital’s surgeons on various health topics such as advanced treatments or procedures and weight loss interventions. Multiple session prenatal classes are held various times throughout the year. The Hospital has integrated health information delivery into the direct delivery online efforts, such as Facebook and e-mail, as this is emerging as an effective way to reach a younger audience. An e-newsletter is sent out to deliver health information directly to users’ inboxes.
- **Online Resource** – The Hospital continues to make a significant investment in the development of our website and in responsible participation in social media. The Hospital has worked to integrate our electronic communication strategies to reach a broad demographic. Key features of the site include an online health directory, drug encyclopedia, health research assistance tool, general health information and information about resources available at the facility. Multiple links have been established with the Hospital’s vendor partners to assist the public in researching specific treatment options. Real time updates related to local disasters, hospital programs or multiple other healthcare related items can be provided through the Hospital’s social media platforms.
- **Social and Health Services** – The Hospital offers assistance before, during and after a health need occurs. The variety of services the Hospital provides include nutritional tours at local groceries by our Registered Dietitian for community members. The tours are specialized for specific groups such as diabetics, senior citizens or families on the go. Other services the Hospital provides include financial counseling, assistance in program enrollment for benefits to which the patient may be entitled and social services. The efforts are expended to ensure that everyone who enters the facility’s doors will be discharged to a safe environment and are aware of the programs available.
- **Community Services** – The Hospital has opened its conference center for use by multiple civic, service and business related entities for educational and meeting space. The two conference rooms are used multiple times each month by outside groups for a wide variety of activities including retreats, seminars, luncheons, interviews and fairs.

### ***Contacting the Hospital’s Financial Management***

This financial report is designed to provide our patients, suppliers, taxpayers and creditors with a general overview of the Hospital’s finances. Questions about this report and requests for additional financial information should be directed to the Hospital administration by telephoning 620.442.2500.

**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas**

**Balance Sheets  
December 31, 2015 and 2014**

**Assets and Deferred Outflows of Resources**

	<b>2015</b>	<b>2014</b> <i>(as restated)</i>
<b>Current Assets</b>		
Cash	\$ 63,472	\$ 117,019
Restricted cash - held under bond indenture	628,978	629,394
Sales tax funds - held by City	359,299	448,588
Patient accounts receivable, net of allowance; 2015 - \$1,749,853, 2014 - \$1,432,390	2,901,751	2,371,760
Estimated amounts due from third-party payers	339,494	82,000
Supplies	746,170	741,642
City of Arkansas City - sales tax receivable	147,957	147,957
Prepaid expenses and other	60,063	96,215
Total current assets	<u>5,247,184</u>	<u>4,634,575</u>
<b>Noncurrent Cash and Assets</b>		
Capital lease interest in unexpended bond proceeds	1,900,119	2,342,520
Held under bond indenture for capital acquisitions - cash	100,000	100,000
Total noncurrent cash and assets	<u>2,000,119</u>	<u>2,442,520</u>
<b>Capital Assets, Net</b>	<u>24,675,467</u>	<u>26,026,023</u>
Total assets	<u>31,922,770</u>	<u>33,103,118</u>
<b>Deferred Outflows of Resources - Pension</b>	<u>252,600</u>	<u>276,174</u>
Total assets and deferred outflows of resources	<u><u>\$ 32,175,370</u></u>	<u><u>\$ 33,379,292</u></u>

## Liabilities, Deferred Inflows of Resources and Net Position

	2015	2014 <i>(as restated)</i>
<b>Current Liabilities</b>		
Outstanding checks in excess of bank balances	\$ 637,790	\$ -
Current maturities of long-term debt	1,034,680	1,149,826
Accounts payable	1,910,455	681,852
Accrued expenses	976,284	1,119,290
Estimated amounts due to third-party payers	39,514	67,000
Unearned grant revenue	2,922	9,956
Total current liabilities	4,601,645	3,027,924
<b>Long-term Debt</b>	23,437,320	23,985,838
<b>Net Pension Liability</b>	4,962,164	4,972,005
Total liabilities	33,001,129	31,985,767
<b>Deferred Inflows of Resources - Pension</b>	986,447	1,364,800
<b>Net Position (Deficit)</b>		
Net investment in capital assets	4,994,575	5,492,994
Restricted - expendable for		
Debt service	628,978	629,394
Capital acquisitions	100,000	100,000
Unrestricted (deficit)	(7,535,759)	(6,193,663)
Total net position (deficit)	(1,812,206)	28,725
Total liabilities, deferred inflows of resources and net position (deficit)	\$ 32,175,370	\$ 33,379,292

**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas  
Statements of Revenues, Expenses and Changes in Net Position  
Years Ended December 31, 2015 and 2014**

	<b>2015</b>	<b>2014</b> <i>(as restated)</i>
<b>Operating Revenues</b>		
Net patient service revenue, net of provision for uncollectible accounts; 2015 - \$1,295,600, 2014 - \$761,286	\$ 16,660,152	\$ 15,845,931
Electronic Health Records Incentive revenue	297,142	790,854
Other	85,937	74,678
Total operating revenues	<u>17,043,231</u>	<u>16,711,463</u>
<b>Operating Expenses</b>		
Salaries and wages	7,520,166	7,186,556
Employee benefits	1,328,686	1,341,286
Purchased services and professional fees	3,524,218	3,016,150
Supplies and other	3,789,431	3,787,562
Depreciation and amortization	1,649,115	1,746,356
Total operating expenses	<u>17,811,616</u>	<u>17,077,910</u>
<b>Operating Loss</b>	<u>(768,385)</u>	<u>(366,447)</u>
<b>Nonoperating Revenues (Expenses)</b>		
Interest income	42,317	53,247
Interest expense	(1,566,762)	(1,650,676)
Noncapital appropriations - City of Arkansas City - sales taxes	875,127	870,684
Noncapital grants and gifts	25,710	19,274
Transfer to City of Arkansas City	(448,938)	-
Total nonoperating revenues (expenses)	<u>(1,072,546)</u>	<u>(707,471)</u>
<b>Decrease in Net Position</b>	(1,840,931)	(1,073,918)
<b>Net Position, Beginning of Year</b>	28,725	7,378,782
<b>Change in Accounting Principle - GASB No. 68</b>	<u>-</u>	<u>(6,276,139)</u>
<b>Net Position, Beginning of Year, as Restated</b>	<u>28,725</u>	<u>1,102,643</u>
<b>Net Position (Deficit), End of Year</b>	<u><u>\$ (1,812,206)</u></u>	<u><u>\$ 28,725</u></u>

**South Central Kansas Regional Medical Center  
d/b/a South Central Kansas Medical Center  
A Component Unit of the City of Arkansas City, Kansas  
Statements of Cash Flows  
Years Ended December 31, 2015 and 2014**

	<b>2015</b>	<b>2014</b> <i>(as restated)</i>
<b>Operating Activities</b>		
Receipts from and on behalf of patients	\$ 15,845,181	\$ 15,204,510
Payments to suppliers and contractors	(5,415,632)	(6,560,052)
Payments to employees and on behalf of employees	(9,356,478)	(8,769,968)
Other receipts, net	383,079	867,233
	<u>1,456,150</u>	<u>741,723</u>
Net cash provided by operating activities		
<b>Noncapital Financing Activities</b>		
Noncapital appropriations - City of Arkansas City - sales taxes	875,127	870,684
Noncapital grants and gifts	18,676	17,868
	<u>893,803</u>	<u>888,552</u>
Net cash provided by noncapital financing activities		
<b>Capital and Related Financing Activities</b>		
Proceeds from the disposal of capital assets	-	13,250
Proceeds from issuance of note payable to City	300,000	-
Principal paid on long-term debt	(1,152,137)	(1,112,158)
Interest paid on long-term debt	(1,573,299)	(1,650,676)
Purchase of capital assets	(110,086)	(292,130)
	<u>(2,535,522)</u>	<u>(3,041,714)</u>
Net cash used in capital and related financing activities		
<b>Investing Activities</b>		
Interest income	42,317	53,247
	<u>42,317</u>	<u>53,247</u>
Net cash provided by investing activities		
<b>Decrease in Cash</b>	(143,252)	(1,358,192)
<b>Cash, Beginning of Year</b>	<u>1,295,001</u>	<u>2,653,193</u>
<b>Cash, End of Year</b>	<u><u>\$ 1,151,749</u></u>	<u><u>\$ 1,295,001</u></u>



**South Central Kansas Regional Medical Center  
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Statements of Cash Flows (Continued)  
Years Ended December 31, 2015 and 2014**

	<u>2015</u>	<u>2014</u> <i>(as restated)</i>
<b>Reconciliation of Cash to the Balance Sheets</b>		
<b>Current Assets</b>		
Cash	\$ 63,472	\$ 117,019
Restricted cash - held under bond indenture	628,978	629,394
Sales tax funds - held by City	359,299	448,588
<b>Noncurrent Cash and Assets</b>		
Held under bond indenture for capital acquisitions - cash	<u>100,000</u>	<u>100,000</u>
Total cash	<u><u>\$ 1,151,749</u></u>	<u><u>\$ 1,295,001</u></u>
<b>Reconciliation of Operating Loss to Net Cash Provided by Operating Activities</b>		
Operating loss	\$ (768,385)	\$ (366,447)
Depreciation and amortization	1,649,115	1,746,356
Loss on sale/disposal of assets	-	1,701
Changes in operating assets and liabilities		
Patient accounts receivable, net	(529,991)	(590,649)
Estimated amounts due to/from third-party payers	(284,980)	(50,772)
Supplies and prepaid expenses	31,624	24,399
Accounts payable and accrued expenses	1,723,387	192,643
Net pension liability	(9,841)	(1,578,666)
Deferred outflows of resources	23,574	(1,642)
Deferred inflows of resources	<u>(378,353)</u>	<u>1,364,800</u>
Net cash provided by operating activities	<u><u>\$ 1,456,150</u></u>	<u><u>\$ 741,723</u></u>
<b>Supplemental Cash Flows Information</b>		
Capital lease obligation incurred for property and equipment	\$ 188,473	\$ -

**South Central Kansas Regional Medical Center  
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**Note 1: Nature of Operations and Summary of Significant Accounting Policies**

***Nature of Operations and Reporting Entity***

South Central Kansas Regional Medical Center d/b/a South Central Kansas Medical Center (Hospital) is an acute care hospital located in Arkansas City, Kansas. The Hospital is a component unit of the City of Arkansas City (City), and the Board of City Commissioners appoints members to the Board of Trustees of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in south central Kansas. The Hospital also operates a home health agency in the same geographic area.

***Basis of Accounting and Presentation***

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions are recognized when all applicable eligibility requirements are met. Government-mandated nonexchange transactions that are not program specific such as city appropriations, property taxes, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position is available.

***Use of Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, deferred outflows of resources, liabilities, deferred inflows of resources and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

***Cash Equivalents***

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2015 and 2014, there were no cash equivalents.

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***Noncapital Appropriations – City of Arkansas City – Sales Tax Revenues***

In 2008, the community of Arkansas City passed a half-cent sales tax to support the construction of the new Hospital facility, purchase of equipment and general operations of the Hospital. The sales tax will be in effect from January 1, 2009 through December 31, 2018. The Hospital received approximately 4.9% in both 2015 and 2014 of its financial support from the sales tax.

Sales tax revenue is recognized based on sales tax collected by the City's retailers in the Hospital's accounting period.

***Risk Management***

The Hospital is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than workers' compensation claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Workers' compensation coverage is provided through a fund managed by the Kansas Hospital Association. The workers' compensation premiums are subject to retrospective adjustment based upon overall performance of the fund. Management believes adequate reserves are in place within the plan to cover claims incurred but not reported, and no additional reserves have been accrued.

***Patient Accounts Receivable***

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

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For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Hospital records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

***Supplies***

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

***Capital Assets***

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Hospital:

Land improvements	10 – 20 years
Buildings and improvements	5 – 50 years
Fixed equipment	3 – 25 years
Major moveable equipment	3 – 20 years

***Compensated Absences***

Hospital policies permit most employees to accumulate vacation, holiday, personal and sick leave benefits that may be realized as paid time off or as a cash payment. Expense and the related liability are recognized as paid time off benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date.

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***Deferred Outflows of Resources***

Deferred outflows of resources represent a consumption of net position that applies to a future period(s) and will not be recognized as an outflow of resources (expense) or reduction of a liability until that time. Deferred outflows of resources consist of contributions from the employer after the measurement date but before the end of the employer's reporting period.

***Deferred Inflows of Resources***

Deferred inflows of resources represent an acquisition of net position that applies to a future period(s) and will not be recognized as an inflow of resources (revenue) or reduction for expense until that time. Deferred inflows of resources consist of the unamortized portion of the net difference between projected and actual earnings on pension plan investments, changes in assumptions and other differences between expected and actual experience.

***Cost-Sharing Defined Benefit Pension Plan***

The Hospital participates in a cost-sharing multiple-employer defined benefit pension plan, the Kansas Public Employees Retirement Savings Plan (KPERS). For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of KPERS and additions to/deductions from KPERS's fiduciary net position have been determined on the same basis as they are reported by KPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

***Net Position***

Net position of the Hospital is classified in three components. Net investment in capital assets consist of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net position are noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Hospital, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net position is remaining net position that does not meet the definition of net investment in capital assets or restricted expendable.

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***Net Patient Service Revenue***

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

***Charity Care***

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

***Electronic Health Records Incentive Program***

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records (EHR) technology. Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The Hospital recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

The Hospital has completed the requirements under the Medicare and Medicaid programs and has recorded revenue of \$297,142 and \$790,854 in the years ended December 31, 2015 and 2014, respectively.

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***Income Taxes***

As an essential government function of the City, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law.

***Implementation of New Accounting Principle***

In fiscal year 2015, the Hospital implemented the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*. The revised requirements establish new financial reporting requirements for state and local governments which provide their employees with pension benefits, including additional note disclosures and required supplementary information. In addition, GASB No. 68 requires a state or local government employer to recognize a net pension liability and changes in the net pension liability, deferred outflows of resources and deferred inflows of resources which arise from other types of events related to pensions. During the transition year, as permitted, beginning balances for deferred outflows of resources and deferred inflows of resources will not be reported, except for deferred outflows of resources related to contributions made after the measurement date of the beginning net pension liability which is required to be reported by GASB No. 71. In accordance with GASB 68, the December 31, 2014, financial statements have been restated to report the adoption of the standard. The effects of the restatement are as follows:

Net position January 1, 2014, as previously reported	\$ 7,378,782
Net pension liability at January 1, 2014	(6,550,671)
Deferred outflows of resources related to contributions made after the June 30, 2013, measurement date	<u>274,532</u>
Net position, beginning of year as restated	<u><u>\$ 1,102,643</u></u>

Decrease in net position for the year ended December 31, 2014, was decreased by \$215,508. Net pension liability and deferred outflows and inflows of resources were also recorded at December 31, 2014, as discussed in *Note 8*.

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**Note 2: Net Patient Service Revenue**

The Hospital recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided.

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

*Medicare.* Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge or per billable service unit. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient skilled nursing services (skilled swing-bed) are paid at prospectively determined per diem rates that are based on the patients' acuity. Home health services are paid on a per episode basis using clinical, diagnostic and other factors. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare Administrative Contractor. Beginning April 1, 2013, a mandatory payment reduction, known as sequestration, of 2% went into effect. Under current legislation, sequestration is scheduled to last until 2025.

*Medicaid.* Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a prospective reimbursement methodology. Due to certain financial and clinical criteria, the Hospital also receives Medicaid disproportionate share (DSH) funding. Medicaid DSH payments were approximately \$699,000 in 2015 and \$292,000 in 2014.

Approximately 58% and 47% of net patient service revenue are from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2015 and 2014, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.



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**Notes to Financial Statements**

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**Note 3: Deposits**

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities or the state of Kansas; bonds of any city, county, school district or special road district of the state of Kansas; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of the deposits.

At December 31, 2015 and 2014, none of the Hospital's bank balances were exposed to custodial credit risk.

***Summary of Carrying Values***

The carrying values of deposits are included in the balance sheets as follows:

	<b>2015</b>	<b>2014</b>
Carrying value		
Deposits	\$ 791,625	\$ 845,588
Petty cash	825	825
	<u>\$ 792,450</u>	<u>\$ 846,413</u>
Included in the following balance sheet captions		
Cash	\$ 63,472	\$ 117,019
Restricted cash - held under bond indenture	628,978	629,394
Held under bond indenture for capital acquisitions - cash	100,000	100,000
	<u>\$ 792,450</u>	<u>\$ 846,413</u>

**South Central Kansas Regional Medical Center  
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**Notes to Financial Statements**

**December 31, 2015 and 2014**

**Note 4: Patient Accounts Receivable**

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2015 and 2014, consisted of:

	<b>2015</b>	<b>2014</b>
Medicare	\$ 627,207	\$ 388,210
Medicaid	316,270	288,056
Other third-party payers	960,284	874,211
Patients	<u>2,747,843</u>	<u>2,253,673</u>
	4,651,604	3,804,150
Less allowance for uncollectible accounts	<u>1,749,853</u>	<u>1,432,390</u>
	<u><u>\$ 2,901,751</u></u>	<u><u>\$ 2,371,760</u></u>

**Note 5: Capital Assets**

Capital assets activity for the years ended December 31, 2015 and 2014, was:

	<b>2015</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ 150,000	\$ -	\$ -	\$ -	\$ 150,000
Land improvements	2,909,460	-	-	-	2,909,460
Buildings	20,975,892	-	-	-	20,975,892
Fixed equipment	262,382	-	-	-	262,382
Major moveable equipment	<u>11,098,662</u>	<u>298,559</u>	<u>-</u>	<u>-</u>	<u>11,397,221</u>
	35,396,396	298,559	-	-	35,694,955
Less accumulated depreciation					
Land improvements	182,508	149,271	-	-	331,779
Buildings	1,604,524	419,606	-	-	2,024,130
Fixed equipment	94,799	26,637	-	-	121,436
Major moveable equipment	<u>7,488,542</u>	<u>1,053,601</u>	<u>-</u>	<u>-</u>	<u>8,542,143</u>
	9,370,373	1,649,115	-	-	11,019,488
Capital Assets, Net	<u><u>\$26,026,023</u></u>	<u><u>\$(1,350,556)</u></u>	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>	<u><u>\$24,675,467</u></u>

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**Notes to Financial Statements**

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	<b>2014</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Transfers</b>	<b>Ending Balance</b>
Land	\$ 150,000	\$ -	\$ -	\$ -	\$ 150,000
Land improvements	2,909,460	-	-	-	2,909,460
Buildings	20,975,892	-	-	-	20,975,892
Equipment	262,382	-	-	-	262,382
Major moveable equipment	10,834,819	286,269	(22,426)	-	11,098,662
	<u>35,132,553</u>	<u>286,269</u>	<u>(22,426)</u>	<u>-</u>	<u>35,396,396</u>
Less accumulated depreciation					
Land improvements	33,237	149,271	-	-	182,508
Buildings	1,184,918	419,606	-	-	1,604,524
Equipment	68,162	26,637	-	-	94,799
Major moveable equipment	6,345,175	1,150,842	(7,475)	-	7,488,542
	<u>7,631,492</u>	<u>1,746,356</u>	<u>(7,475)</u>	<u>-</u>	<u>9,370,373</u>
Capital Assets, Net	<u>\$27,501,061</u>	<u>\$(1,460,087)</u>	<u>\$ (14,951)</u>	<u>\$ -</u>	<u>\$26,026,023</u>

**Note 6: Long-term Debt**

The following is a summary of long-term debt transactions for the Hospital for the years ended December 31, 2015 and 2014:

	<b>2015</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Payments</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Long-term debt					
Capital lease obligations	\$ 25,135,664	\$ 188,473	\$ 1,052,137	\$24,272,000	\$ 834,680
Note payable to City	-	300,000	100,000	200,000	200,000
	<u>\$ 25,135,664</u>	<u>\$ 488,473</u>	<u>\$ 1,152,137</u>	<u>\$24,472,000</u>	<u>\$ 1,034,680</u>
	<b>2014</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Payments</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Long-term debt					
Capital lease obligations	\$ 26,247,822	\$ -	\$ 1,112,158	\$25,135,664	\$ 1,149,826

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***Note Payable to City***

The note payable to City is due August 2016, with principal of \$25,000 payable monthly. The note is an interest free loan as the Hospital is a component unit of the City and City management did not feel it was necessary to charge interest to itself.

***Capital Lease Obligations***

In 2009, the Hospital entered into an agreement with the Public Building Commission (PBC) of the City of Arkansas City, Kansas to issue bonds to finance construction of a replacement facility. The bonds bear interest ranging from 4.00% to 7.00% and are due semi-annually in increasing principal amounts with final bonds maturing September 1, 2038. The Hospital, acting as its own trustee, is required to maintain specific principal and interest accounts. The PBC holds the required bond reserve account. The actual principal and interest payments are then made to the PBC which remits the payments to the state treasurer's office and then the bondholders are paid by the state. Accordingly, the facility and bond indebtedness have been included in the financial statements as assets and liabilities of the Hospital. The bonds are secured by a first and prior lien upon the gross revenues of the Hospital. This agreement is accounted for as a capital lease obligation by the Hospital. All covenants within the agreements must be met primarily by the Hospital.

Bonds issued may be redeemed in advance of their maturity at 100% of face value.

The bond indentures require certain covenants be met during each year. Those covenants require income available for future debt service of 1.0, the facility must be maintained and insured, and monthly deposits must be made to the trustee account. As of December 31, 2015, the Hospital did not meet the debt service coverage covenant. Under the bond agreement, the Hospital is required to hire a consultant to help determine a plan to get the Hospital back to a financial position where they are in compliance required covenants.

The Hospital entered into an agreement with the City in 2010 (at which time costs and repayment terms were unknown) to repay costs related to the extension of city utilities, *i.e.*, sewer, water and street. The Hospital and City entered into repayment terms in December 2013 whereas the Hospital would make monthly payments to the City beginning December 15, 2013, in the amount of \$17,696 for 12 consecutive months. The monthly payment increases to \$17,934 for December 15, 2014, and remains at that level for the next 108 months. The monthly payment drops to \$10,304 beginning December 15, 2023, and continues at that level for the next 120 months or until final payoff of the extension costs. The City is charging the Hospital 2.152% interest on the payment of the extension costs in order to cover the City's costs related to the bonds that were issued to fund the expansion work.

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**December 31, 2015 and 2014**

The Hospital is also obligated under other capital leases for building improvements and equipment. All assets under capital leases at December 31, 2015 and 2014, totaled \$22,604,040 and \$24,573,221, respectively, net of accumulated depreciation of \$3,622,934 and \$4,403,106, respectively. The following is a schedule by year of future minimum lease payments under the capital leases including interest at rates of 4.00% to 7.00% together with the present value of the future minimum lease payments as of December 31, 2015:

Year Ending December 31,	
2016	\$ 2,367,408
2017	2,157,176
2018	2,100,714
2019	2,104,254
2020	2,100,134
2021-2025	10,313,983
2026-2030	10,049,995
2031-2035	9,793,530
2036-2038	5,656,800
Total minimum lease payments	<u>46,643,994</u>
Less amount representing interest	<u>22,371,994</u>
Present value of future minimum lease payments	<u>\$ 24,272,000</u>

**Note 7: Medical Malpractice Claims**

The Hospital purchases medical malpractice insurance which provides \$200,000 of coverage for each medical incident and \$600,000 of aggregate coverage for each policy year. The policy is a claims-made policy, which means the policy only covers claims made and reported to the insurer during the policy term, regardless of when the incident giving rise to the claim occurred. The Kansas Health Care Stabilization Fund provides an additional \$800,000 of coverage for each medical incident and \$2,400,000 of aggregate coverage for each policy year.

Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

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**Note 8: Pension Plan**

***Plan Description***

The Kansas Public Employees Retirement System Plan is an umbrella organization administering the following three statewide retirement systems under one plan as provided by K.S.A. 74, Article 49: Kansas Public Employees Retirement System (KPERS), Kansas Police and Fire Retirement System and Kansas Retirement System for Judges.

The KPERS plan is a cost-sharing multiple-employer defined benefit plan. KPERS is intended to be a qualified retirement plan under Section 401(a) of the Code. Information relating to KPERS, including stand-alone financial statements, is available by writing to KPERS, 611 South Kansas Avenue, Suite 100, Topeka, Kansas 66603-3869 or accessing the internet at [www.KPERS.org](http://www.KPERS.org).

KPERS makes separate calculations for pension-related amounts for the following four groups participating in the plan:

- State/School
- Local
- Police and Firemen
- Judges

The Hospital's employees participate in the Local group.

***Benefits Provided***

Retirement benefits for employees are calculated based on the credited service, final average salary and a statutory multiplier. KPERS has two levels of benefits depending on retirement age and years of credited service. Tier 1 benefits are for members who are age 65 or age 62 with ten years of credited service or of any age when combined age and years of credited service equal 85 "points." Tier 2 benefits are for members who are age 65 with five years of credited service or age 60 with 30 years of credited service. Tier 1 members receive a participating service credit of 1.75% of the final average salary for years of service prior to January 1, 2014. Participating service credit is 1.85% of final average salary for years of service after December 31, 2013. Tier 2 members retiring on or after January 1, 2012, participating service credit is 1.85% for all years of service.

Early retirement is permitted at the age of 55 and ten years of credited service. Benefits are reduced by 0.2% per month for each month between the ages of 60-62, plus 0.6% for each month between the ages of 55 and 60 for Tier 1 members. For Tier 2 members, benefits are reduced actuarially for each early commencement. The reduction factor is 35% at the age of 60 and 57.5% at age 55. If the member has 30 years of credited service, the early retirement reduction is less (50% of regular reduction). The plan also provides disability and death benefits to plan members and their beneficiaries.

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The terms of the plan provide for annual 2% cost-of-living adjustment for Tier 2 members who retired prior to July 1, 2012, beginning the later of age of 65 or the second July 1 after retirement date. Other participants do not receive a cost-of-living adjustment.

***Contributions***

The law governing KPERS requires an actuary to make an annual valuation of the liabilities and reserves and a determination of the contributions required to discharge the KPERS liabilities. The actuary then recommends to the KPERS Board of Trustees the state wide employer-contribution rates required to maintain the three systems on the actuarial reserve basis. Prior to January 1, 2014, Tier 1 participants were required to contribute 4% of their annual pay. Effective January 1, 2014, the rate was raised to 5% with an increase in the benefit multiplier to 1.85% beginning January 1, 2014, for future years of service only. Effective January 1, 2015, the contribution rate was raised to 6%. Tier 2 participants are required to contribute 6% of compensation. The Hospital's contractually required contribution rate for the years ended December 31, 2015 and 2014, was 9.48% and 8.84% of annual payroll, respectively. The employer contribution is actuarially determined as an amount that, when combined with employee contributions, is expected to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability.

The Hospital's contributions to KPERS for the years ended December 31, 2015 and 2014, were \$575,911 and \$557,877, respectively.

***Pension Liabilities, Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions***

At December 31, 2015 and 2014, the Hospital reported a liability of \$4,962,164 and \$4,972,005, respectively, for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015 and 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of December 31, 2014 and 2013, respectively, rolled forward to June 30, 2015 and 2014, respectively. The Hospital's proportion of the net pension liability was based on the ratio of the Hospital's actual contributions to total employer and non-employer actual contributions of the group for the respective measurement periods. At June 30, 2015, the Hospital's proportion was 0.377913%, which was a decrease of 0.026048% from its proportion measured as of June 30, 2014, of 0.403961%. At June 30, 2013, the proportion was 0.430376%.

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**December 31, 2015 and 2014**

For the years ended December 31, 2015 and 2014, the Hospital recognized pension expense of \$190,733 and \$342,896, respectively. At December 31, 2015 and 2014, the Hospital reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<b>2015</b>	
	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience	\$ -	\$ 140,469
Net difference between projected and actual earnings on pension plan investments	-	193,160
Changes of assumptions	-	69,352
Changes in proportion	-	583,466
Hospital's contributions subsequent to the measurement date	252,600	-
Total	<u>\$ 252,600</u>	<u>\$ 986,447</u>

  

	<b>2014</b>	
	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience	\$ -	\$ 140,572
Net difference between projected and actual earnings on pension plan investments	-	891,253
Changes in proportion	-	332,975
Hospital's contributions subsequent to the measurement date	276,174	-
Total	<u>\$ 276,174</u>	<u>\$ 1,364,800</u>



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At December 31, 2015, the Hospital reported \$252,600 as deferred outflows of resources related to pension contributions made subsequent to the measurement date that will be recognized as a reduction of the net pension liability in the year ending December 31, 2016. Other amounts reported as deferred inflows of resources at December 31, 2015, related to pensions will be recognized in pension expense as follows:

2016	\$ (286,655)
2017	(286,655)
2018	(286,655)
2019	(60,864)
2020	<u>(65,618)</u>
	<u><u>\$ (986,447)</u></u>

***Actuarial Assumptions***

The total pension liability in the December 31, 2014 and 2013, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3%
Salary increases	4% to 16%, including inflation (4% to 12.5% for 2013)
Investment rate of return	8%, net of pension plan investment expense, including inflation

Mortality rates were based on the RP-2000 Healthy Annuitant table, as appropriate with adjustments for mortality improvements based on Scale AA.

The actuarial assumptions used in the December 31, 2014, valuation was based on the results of an actuarial experience study for the three-year period ended December 31, 2012.

The actuarial assumptions used in the December 31, 2013 and 2012, valuations were based on the results of an actuarial experience study conducted for the three-year period ended December 31, 2009.

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The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following tables:

<b>Asset Class</b>	<b>2015</b>	
	<b>Target Allocation</b>	<b>Long-term Expected Real Rate of Return</b>
Global equity	47%	6%
Fixed income	13%	0.80%
Yield driven	8%	4.20%
Real return	11%	1.70%
Real estate	11%	5.40%
Alternatives	8%	9.40%
Short-term investments	2%	-0.50%
	<u>100%</u>	
<b>Asset Class</b>	<b>2014</b>	
	<b>Target Allocation</b>	<b>Long-term Expected Real Rate of Return</b>
Global equity	47%	6.30%
Fixed income	14%	0.85%
Yield driven	8%	5.50%
Real return	11%	3.75%
Real estate	11%	6.65%
Alternatives	8%	9.50%
Short-term investments	1%	0.00%
	<u>100%</u>	

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***Discount Rate***

The discount rate used to measure the total pension liability was 8% for the years ended December 31, 2014 and 2013. The projection of cash flows used to determine the discount rate assumed that member contributions will be made at the contractually required rate. Participating employer contributions do not necessarily contribute the full actuarial determined rate. Based on legislation passed in 1993, the employer contribution rates certified by KPERS' Board of Trustees for these groups may not increase by more than the statutory cap. The expected KPERS employer statutory contribution was modeled for future years, assuming all actuarial assumptions are met in future years. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

***Sensitivity of the Hospital's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate***

The Hospital's proportionate share of the net pension liability has been calculated using a discount rate of 8%. The following presents the Hospital's proportionate share of the net pension liability calculated using a discount rate 1% higher and 1% lower than the current rate.

	<b>1% Decrease (7%)</b>	<b>Current Discount Rate (8%)</b>	<b>1% Increase (9%)</b>
Hospital's proportionate share of the net pension liability (2015)	\$ 7,044,056	\$ 4,962,164	\$ 3,197,130
Hospital's proportionate share of the net pension liability (2014)	\$ 7,139,865	\$ 4,972,005	\$ 3,135,241

***Pension Plan Fiduciary Net Position***

Detailed information about the pension plan's fiduciary net position is available in the separately issued KPERS' financial report.

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**Note 9: Contingencies**

***Litigation***

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Hospital's self-insurance program (discussed elsewhere in these notes) or by commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

## **Required Supplementary Information**

**South Central Kansas Regional Medical Center  
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Schedule of the Hospital's Proportionate Share of the Net Pension Liability  
Kansas Public Employees Retirement System Plan  
Last Ten Fiscal Years**

	<b>2015 *</b>	<b>2014 *</b>
Hospital's proportion of the net pension liability	0.377913%	0.403961%
Hospital's proportionate share of the net pension liability	\$ 4,962,164	\$ 4,972,005
Hospital's covered-employee payroll	\$ 6,265,319	\$ 6,895,637
Hospital's proportionate share of the net pension liability as a percentage of its covered-employee payroll	79.20%	72.10%
Plan fiduciary net position as a percentage of the total pension liability	64.95%	66.60%

**Note to Schedule:** This schedule is intended to show a 10-year trend. Additional years will be reported as they become available.

\*The amounts presented for each fiscal year are as of the measurement date (June 30 of each fiscal year).

**South Central Kansas Regional Medical Center  
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Schedule of the Hospital's Contributions  
Kansas Public Employees Retirement System Plan  
Last Ten Fiscal Years**

	<u>2015 *</u>	<u>2014 *</u>
Contractually required contribution	\$ 575,911	\$ 557,877
Contribution in relation to the contractually required contribution	<u>575,911</u>	<u>557,877</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>
Hospital's covered-employee payroll	\$ 6,265,319	\$ 6,895,637
Contributions as a percentage of covered-employee payroll	9.19%	8.09%

**Note to Schedule:** This schedule is intended to show a 10-year trend. Additional years will be reported as they become available.

\*The amounts presented for each fiscal year are as of the most recent fiscal year-end (December 31).

**South Central Kansas Regional Medical Center  
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Notes to Required Supplementary Information  
December 31, 2015 and 2014**

**Changes of Benefit and Funding Terms:** The following changes to the plan provisions as of January 1 2015 and 2014, as listed below, were reflected in the valuation performed:

Effective January 1, 2014, KPERS Tier 1 member's employee contribution rate increased to 5.0% with an increase in benefit multiplier to 1.85% for future years of service. Effective January 1, 2015, the rate increased to 6.0% with the benefit multiplier continuing at 1.85% for future years of service. For Tier 2 members retiring after July 1, 2012, the cost of living adjustment is eliminated but members will receive a 1.85% multiplier for all years of service.



## **Supplementary Information**

**South Central Kansas Regional Medical Center  
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Schedules of Net Patient Service Revenues  
Years Ended December 31, 2015 and 2014**

	2015		
	Inpatient	Outpatient	Total
<b>Nursing Services</b>			
Nursing, dietary and room services	\$ 2,034,476	\$ -	\$ 2,034,476
Observation	-	297,865	297,865
Intensive care	214,054	-	214,054
Nursery	215,517	-	215,517
Skilled swing-bed	115,140	-	115,140
	<u>2,579,187</u>	<u>297,865</u>	<u>2,877,052</u>
<b>Other Professional Services</b>			
Operating room	675,220	2,524,193	3,199,413
Delivery room	601,914	131,036	732,950
Anesthesiology	43,585	30,382	73,967
Radiology	98,391	823,413	921,804
CT scans	131,365	1,609,548	1,740,913
Magnetic resonance imaging	23,672	1,031,124	1,054,796
Nuclear medicine	6,107	179,960	186,067
Ultrasound	208,314	717,343	925,657
Laboratory	917,849	3,018,891	3,936,740
Intravenous therapy	710,454	656,340	1,366,794
Respiratory therapy	526,355	149,711	676,066
Physical therapy	97,515	471,743	569,258
Occupational therapy	40	70	110
Speech therapy	4,902	13,320	18,222
Electrocardiology	21,730	102,934	124,664
Central supply	933,153	1,667,499	2,600,652
Pharmacy	1,059,629	1,819,268	2,878,897
Outpatient surgery	-	23,988	23,988
Sleep study revenue	-	-	-
Emergency room	367,034	3,446,572	3,813,606
Downtown clinic	-	1,865,380	1,865,380
Physician clinics	-	3,644,518	3,644,518
	<u>6,427,229</u>	<u>23,927,233</u>	<u>30,354,462</u>
	<u>\$ 9,006,416</u>	<u>\$ 24,225,098</u>	<u>33,231,514</u>
<b>Provision for Uncollectible Accounts</b>			1,295,600
<b>Contractual and Other Adjustments</b>			<u>15,275,762</u>
<b>Net Patient Service Revenue</b>			<u>\$ 16,660,152</u>

2014		
Inpatient	Outpatient	Total
\$ 1,746,852	\$ -	\$ 1,746,852
-	445,780	445,780
244,367	-	244,367
205,732	-	205,732
181,546	-	181,546
<u>2,378,497</u>	<u>445,780</u>	<u>2,824,277</u>
759,185	3,009,318	3,768,503
594,084	91,687	685,771
-	-	-
91,109	789,723	880,832
138,701	1,508,607	1,647,308
27,262	1,022,702	1,049,964
4,382	176,538	180,920
234,543	677,767	912,310
947,445	2,910,343	3,857,788
710,375	610,470	1,320,845
513,512	149,591	663,103
117,723	533,800	651,523
-	-	-
4,110	13,171	17,281
29,684	117,752	147,436
1,176,746	1,929,925	3,106,671
1,094,830	1,505,848	2,600,678
-	15,322	15,322
-	96,492	96,492
287,332	2,354,233	2,641,565
-	1,056,554	1,056,554
-	4,312,325	4,312,325
<u>6,731,023</u>	<u>22,882,168</u>	<u>29,613,191</u>
<u>\$ 9,109,520</u>	<u>\$ 23,327,948</u>	32,437,468
		761,286
		<u>15,830,251</u>
		<u>\$ 15,845,931</u>

**South Central Kansas Regional Medical Center  
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Schedules of Contractual Allowances and Other Revenue  
Years Ended December 31, 2015 and 2014**

**Contractual Allowances**

	<b>2015</b>	<b>2014</b>
Medicare	\$ 6,764,836	\$ 6,909,488
Medicaid	3,508,970	3,752,647
Medicaid – Disproportionate share adjustment	(698,963)	(292,592)
Blue Cross	2,018,223	1,982,582
Commercial	3,034,429	2,919,871
Charity care	379,815	298,953
Other	268,452	259,302
	<u>\$ 15,275,762</u>	<u>\$ 15,830,251</u>

**Other Revenue (Expense)**

	<b>2015</b>	<b>2014</b>
Cafeteria sales	\$ 47,733	\$ 49,112
Employee pharmacy sales	2,744	2,636
Rental income	10,850	13,500
Loss from sale/disposal of assets	-	(1,701)
Miscellaneous	24,610	11,131
	<u>\$ 85,937</u>	<u>\$ 74,678</u>

**South Central Kansas Regional Medical Center  
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Schedules of Operating Expenses  
Years Ended December 31, 2015 and 2014**

	<b>2015</b>			<b>2014</b>		
	<b>Salaries</b>	<b>Other</b>	<b>Total</b>	<b>Salaries</b>	<b>Other</b>	<b>Total</b>
<b>Nursing Services</b>						
Nursing service	\$ 873,778	\$ 310,240	\$ 1,184,018	\$ 923,639	\$ 119,285	\$ 1,042,924
Intensive care	169,039	6,996	176,035	203,772	8,761	212,533
	<u>1,042,817</u>	<u>317,236</u>	<u>1,360,053</u>	<u>1,127,411</u>	<u>128,046</u>	<u>1,255,457</u>
<b>Other Professional Services</b>						
Operating room	327,128	192,326	519,454	319,264	153,028	472,292
Delivery room	302,482	58,709	361,191	303,434	60,146	363,580
Anesthesiology	182,219	466,211	648,430	194,708	351,696	546,404
Radiology	262,795	240,218	503,013	502,514	248,416	750,930
CT scans	38,620	131,114	169,734	-	126,583	126,583
Magnetic resonance imaging	65,896	111,886	177,782	-	119,328	119,328
Nuclear medicine	25,344	15,373	40,717	-	15,392	15,392
Ultrasound	141,115	9,879	150,994	-	10,831	10,831
Laboratory	469,200	585,174	1,054,374	457,806	561,873	1,019,679
Intravenous therapy	-	68	68	-	522	522
Respiratory therapy	228,799	16,552	245,351	228,346	18,001	246,347
Physical therapy	236,950	5,360	242,310	259,348	17,443	276,791
Electrocardiology	-	-	-	-	1,050	1,050
Cardiac rehab	-	-	-	690	5	695
Central supply	30,669	745,332	776,001	30,862	919,657	950,519
Pharmacy	212,534	828,108	1,040,642	218,954	677,428	896,382
Outpatient surgery	81,584	5,974	87,558	90,679	4,839	95,518
Sleep study lab	-	-	-	-	15,124	15,124
Emergency room	824,959	628,698	1,453,657	897,861	628,580	1,526,441
Downtown clinic	708,215	479,786	1,188,001	356,086	227,199	583,285
Physician clinic	453,010	37,049	490,059	448,471	70,365	518,836
	<u>4,591,519</u>	<u>4,557,817</u>	<u>9,149,336</u>	<u>4,309,023</u>	<u>4,227,506</u>	<u>8,536,529</u>

**South Central Kansas Regional Medical Center  
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Schedules of Operating Expenses (Continued)  
Years Ended December 31, 2015 and 2014**

	<b>2015</b>			<b>2014</b>		
	<b>Salaries</b>	<b>Other</b>	<b>Total</b>	<b>Salaries</b>	<b>Other</b>	<b>Total</b>
<b>General Services</b>						
Plant operation	\$ 137,219	\$ 381,963	\$ 519,182	\$ 146,752	\$ 413,566	\$ 560,318
Laundry	-	8,321	8,321	22	7,436	7,458
Housekeeping	36,333	6,818	43,151	645	6,554	7,199
Dietary	25,396	599,616	625,012	302	694,855	695,157
	<u>198,948</u>	<u>996,718</u>	<u>1,195,666</u>	<u>147,721</u>	<u>1,122,411</u>	<u>1,270,132</u>
<b>Administration Services</b>						
Administration and general	906,813	697,799	1,604,612	909,571	675,246	1,584,817
Business office	217,551	414,244	631,795	276,666	347,609	624,275
Purchasing	56,935	29,825	86,760	56,988	39,302	96,290
Nursing administration	268,819	11,886	280,705	145,321	17,183	162,504
Medical records	161,807	169,596	331,403	138,513	155,710	294,223
Public relations	74,957	118,528	193,485	75,342	90,699	166,041
	<u>1,686,882</u>	<u>1,441,878</u>	<u>3,128,760</u>	<u>1,602,401</u>	<u>1,325,749</u>	<u>2,928,150</u>
<b>Employee Benefits</b>		<u>1,328,686</u>	<u>1,328,686</u>		<u>1,341,286</u>	<u>1,341,286</u>
<b>Depreciation</b>		<u>1,649,115</u>	<u>1,649,115</u>		<u>1,746,356</u>	<u>1,746,356</u>
	<u>\$ 7,520,166</u>	<u>\$ 10,291,450</u>	<u>\$ 17,811,616</u>	<u>\$ 7,186,556</u>	<u>\$ 9,891,354</u>	<u>\$ 17,077,910</u>